

SEP 80

Chief, Examination Division
Nashville District Office
Attn: Raymond Dunn, Estate Tax Attorney

Chief, Branch 4, Passthroughs and Special Industries
CC:P&SI:4

Technical Assistance under Code Section 2056
Control No: TR-45-1184-91

On July 10, 1991, you requested technical assistance on computation of a marital deduction for an elective share made under Tennessee law. Specifically, you ask:

- 1) Is a surviving spouse's elective share, under Tennessee law, decreased by secured debts of the decedent?
- 2) If so, by how much is the surviving spouse's elective share decreased?

Issue 1:

Section 31-2-101 of the Tennessee Code Annotated (TCA) provides that when any person shall die intestate, after the payment of debts and charges against the estate, his property passes to his heirs as prescribed in the following sections of this chapter. Any part of the estate of a decedent not effectively disposed of by his will passes to his heirs in the same manner.

Section 31-2-103(b) of the TCA provides that the net estate shall include all of the decedent's property reduced by funeral and administration expenses, homestead, exemptions, and year's support.

Section 31-2-104(a) of the TCA provides that the intestate share of the surviving spouse is: (1) If there is no surviving issue of the decedent, the entire intestate estate; or (2) If there are surviving issue of the decedent, either one-third (1/3) or a child's share of the entire intestate estate, whichever is greater.

Section 31-4-101(a) of the TCA provides that a decedent's surviving spouse has the right to elect to take an elective share. The elective share is one third (1/3) of the decedent's net estate as defined in subsection (b) hereof. The right to elect an elective share is available to the surviving spouse of an intestate decedent or if the surviving spouse elects against

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the decedent's will. When the elective share is determined, it is exempt from the unsecured debts of the decedent incurred after April 1, 1977. In determining the elective share, it is not reduced by any estate or inheritance taxes.

Section 31-4-101(b) of the TCA provides that the net estate includes all of the decedent's real and personal property subject to disposition under the terms of the decedent's will or the laws of intestate succession reduced by funeral and administration expenses, homestead, exemptions and year's support.

In Phipps v. Watts, 781 S.W. 2d 863 (Tenn. Ct. App. 1989), the court held that the exemptions mentioned in section 31-4-101 of the TCA are the exemptions for personal property provided for in section 30-2-101. Section 30-2-101 provides, in part, that the surviving spouse of an intestate decedent, or the surviving spouse of a testate decedent who elects to take against the will, is entitled absolutely to certain specified personal property without regard to its value. In addition, the property subject to 30-2-101 in no case is to be liable for the payment of claims against the estate. Other provisions for surviving spouses of intestate decedents or spouses electing against a will include section 30-2-102, which provides a reasonable allowance in money (or property) out of the estate for the spouse's maintenance during the period of one year after the death of the decedent which is specifically exempt from all claims of the estate.

Section 31-4-101 of the TCA was revised in 1985, the prior section reads as follows:

The surviving spouse shall have a right of election to take an elective share of one-third (1/3) of decedent's net estate as defined by section 31-2-103(b)¹. Such elective share, when so determined, shall be exempt from the debts and charges of the decedent incurred after April 1, 1977.

The current statute for the elective share specifically exempts the elective share from unsecured debts incurred after April 1, 1977, and from estate and inheritance taxes. This is in contrast to the pre-1985 version that provided the elective share was exempt from all debts and charges of the decedent incurred after April 1, 1977. The legislature has exempted certain

¹ Section 31-2-103(b), the definition of net estate, did not change in 1985 when the changes to section 31-4-101 were made.

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property (personal property under 30-2-101 and one-year allowance under 30-2-102) passing to a surviving spouse from all debts and charges and neither provision was changed in 1985. Lacking guidance from the Tennessee Supreme Court or the Tennessee legislature to the contrary, we believe the intention of the Tennessee legislature in 1985, was to exempt the elective share only from the unsecured debts incurred after April 1, 1977 and not other debts.

Issue 2:

Section 2056(a) of the Internal Revenue Code provides that, for purposes of the estate tax, the value of the taxable estate shall, except as limited by subsection (b), be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

Section 2056(b)(2) of the Code provides that where the assets (included in the decedent's gross estate) out of which, or the proceeds of which, an interest passing to the surviving spouse may be satisfied include a particular asset or assets with respect to which no deduction would be allowed if such asset or assets passed from the decedent to such spouse, then the value of such interest passing to such spouse, shall, for purposes of subsection (a), be reduced by the aggregate value of such particular assets.

Section 2056(b)(4) of the Code provides, in part, that in determining the value of any interest in property passing to the surviving spouse for which a marital deduction is allowed, where such interest or property is encumbered in any manner, or where the surviving spouse incurs any obligation imposed by the decedent with respect to the passing of such interest, such encumbrance or obligation shall be taken into account in the same manner as if the amount of a gift to such spouse of such interest were being determined.

Section 30-2-305 of the TCA provides that every debtor's property, except such as may be specially exempt by law, shall be considered assets for the satisfaction of all a decedent's just debts.

Section 35-50-112 of the TCA provides that no executor, trustee, or other fiduciary may take, or refuse to take, any

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action, or make or retain any investment, the result of which would defeat an otherwise available marital deduction under the Internal Revenue Code or under the laws of the state the Tennessee, if the obvious and expressed intent of the testator or settlor was to take advantage of this deduction. After May 23, 1977, this section applies to all acts or investments, by all executors, trustees, or other fiduciaries, as to all wills and trusts, whenever these instruments were executed.

An elective share is in the nature of a general legacy in that the interest is in one-third of the net estate and may be paid out of any combination of assets as opposed to any specific asset. In accordance with section 31-4-101 of the TCA, the elective share is exempt from unsecured debts of a decedent accruing after 4/1/77. Therefore, only a proportionate share of the secured debts would be allocable against the surviving spouse's elective share.

Esther Woodworth of this office is familiar with this case and can be reached at (FTS) 343-8554.

(signed) Richard R. Grosgebauer

Richard Grosgebauer